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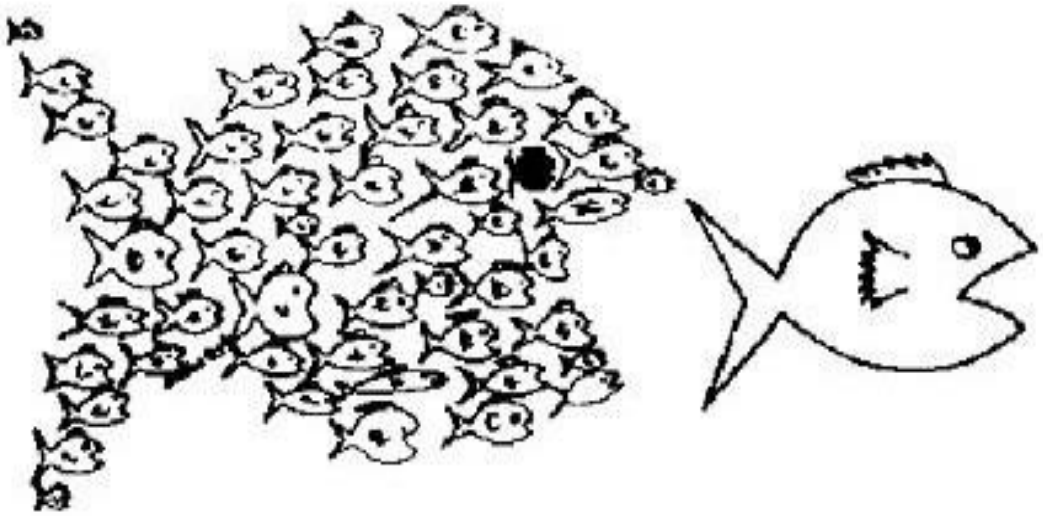
CLASS ACTION IN INDIA



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Introduction

A Class Action, speaking simply, is where a class or group of people with a common grievance join hands in order to seek relief. It is a cost effective procedural device whereby few people can sue for the advantage of a larger group. India was familiar with class action only in the form of representative suit under the Code of Civil Procedure, 1908 or Public Interest Litigation, each having their own limitations. The concept of a class action has been part of the legal system of other countries since decades. However, this valuable tool was not available to the stakeholders in India until the introduction of the Companies Act, 2013 ("***Companies Act***"). One may attribute the special provision of class action in the Companies Act to the Satyam Case of 2009.

In Satyam's case, the founder chairman of Satyam Computer Services Limited ("***Satyam***"), one of the country's biggest information technology company, confessed to a manipulation of facts and figures worth billions in Satyam's books of accounts. Although, the laws of India had provided a platform to the stakeholders to raise their voice, they all proved to be insufficient in the aforesaid case. The investors of Satyam in the US were successful in claiming damages through a class action suit. While the Indian laws were able to punish the wrongdoer, due to absence of a similar recourse in our statutes (i.e. law enabling collective claim against defendants), the Indian investors were unable to recover their losses. As a result, an urgent need to restore the faith of the investors and stringent corporate governance was realized by the Central Government. This led to, amongst others, the long awaited legal recognition to class action in India, through the Companies Act.

Class Action – Section 245

Under the Companies Act, the concept of class action finds its place in Chapter XVI for prevention of oppression and mismanagement, wherein the neighbouring provisions have been made with a similar objective i.e. protection of interests of all stakeholders. The Legislature through Section 245 of the Companies Act, has given a right to certain members and depositors of the

company to collectively proceed against the company, the directors, auditors, or any advisor or expert who engage in any wrongful, unlawful and fraudulent act or omission or conduct on their part in relation to a company ("***Class Action***"). As per the Companies Act, the minimum number of members required to file a Class Action are: (i) in case of a company having share capital, atleast 100 members or the prescribed percentage of total number of members, whichever is less or any member or members holding the prescribed percentage of shareholding in the company, subject to a condition that the member or members have paid all calls and other sums due on his or their shares; and (ii) in case of company not having share capital, atleast 1/5th of the total members of the company. In case of depositors, the minimum requirement is of atleast 100 depositors or the prescribed percentage of total number of depositors, whichever is less, or any depositor or depositors to whom the company owes the prescribed percentage of the total deposits of the company.

The draft rules on the concerned chapter suggest the prescribed percentage of total number of members and depositors to be 10%, which is similar to the requirement under Section 241 of the Companies Act. As such, we can (for the moment, safely) assume that the official prescribed percentage will be on the same lines.

Under Section 245 of the Companies Act, the members and depositors can collectively approach the National Company Law Tribunal ("***Tribunal***") to seek an order for restraining a company from committing an act which is ultra vires of or is in breach of the constitutional documents of the company, declaring a resolution altering the Memorandum and Articles of the company as void if such resolution is passed by superseding material facts or through a misstatement, restraining the company or director from doing any act which is contrary to any law, restraining the company from doing an act contrary to any resolution passed by the members etc. A Class Action provides a redressal mechanism for the stakeholders of the company whereby they can seek compensation from the directors, auditors, experts etc. and make them liable for their wrongful conduct and acts. Section 245 also allows representative action by any person, group of persons or any association on behalf of persons affected under the Companies Act. The shareholders of a company can also take advantage of Section 245 to take a derivative action against any director of the company under Section 166 (Duties of the Directors) of the Companies Act.

The Tribunal, before admitting an application, is required to consider various factors such as whether applicants are acting on good faith, whether any third person apart from the ones specified in the Companies Act is involved, whether cause of action is one which the member or depositor can pursue in his own right, whether the class has so many members that joining them individually would be impractical making a Class Action desirable, etc. The Companies Act does not encourage the members or depositors to use this mechanism for resolving their personal grievances and where an alternate remedy is already available under the Companies Act. It is the responsibility of the Tribunal to ensure that the application in question fulfills the eligibility parameters set out in the Companies Act and is made for a genuine cause.

While considering the desirability of an individual or separate action as opposed to a Class Action, the Tribunal may take into account, in particular, whether admitting separate actions by member or members or depositor or depositors would create a risk of:-(a) inconsistent or varying adjudications in such separate actions; or (b) adjudications that, as a practical matter, would be dispositive of the interests of the other members; and (c) adjudications which would substantially impair or impede the ability of other members of the class to protect their interests.

Once an application has been admitted, the Tribunal is required to cause publication of a notice to all the members of such class containing the details of the application. The Tribunal also allows the consolidation of all similar applications prevalent in different jurisdiction into one single application.

Though the National Company Law Tribunal Rules, 2016, provides an additional insight as to the workings of Section 245, since no formal rules in this respect have been issued by the Ministry of Corporate Affairs yet, several aspects of the provision are yet to be clarified.

Class Action vs. Oppression and Mismanagement

The shareholders of a company can also avail a remedy under Section 241 (*Application to Tribunal for relief in cases of oppression etc.*) of the Companies Act, which allows relief in cases where the affairs of the company have been conducted in a manner prejudicial to public interest or oppressive to any other member or in a manner prejudicial to the interest of the company. However, Section 241 limits its protection to the shareholders of a company, while Section 245 also includes depositors in its purview. Although, as compared to Section 245, the scope of remedies available under Section 241 is much wider (*such as order for purchase of shares by any member, restrictions on transfer or allotment, termination or modification of an agreement, removal or appointment of director etc.*), Section 245 is much more generous with an award for damages and compensation to the applicants. Any order made under Section 245 is in nature of rem and is binding even on those members or depositors who are not party to the application as opposed to an order of oppression and mismanagement which is only binding on the parties to the application. While a Class Action can be invoked in case of any act prejudicial to the interest of the members, the depositors or the company; in case of oppression and management, public interest is also taken into account.

The Companies Act has equipped the shareholders with strong weapons in the form of Section 241 to Section 245 which can be used to make the delinquent officers accountable for their decisions and for enforcement of the corporate law. In wake of this new empowerment of the stakeholders, the corporate officers will have to become more prudent with their operations to secure themselves against a Class Action.

The concept of class action is at a very nascent stage in India. The concept is yet to be evolved and adapted as per the practical application and the changing market trends. Although other remedies under the Companies Act have plethora of precedents to guide the applicants, India is yet to develop its own library of judgments to rely on, for the purpose of Class Action. One may have to refer the judgments of foreign countries on this concept for some guidance till that time.

Our View

The provision of Class Action in the Companies Act, ensures that the management of a company prioritizes the interest of the stakeholders and the company against its own and make them answerable to the stakeholders of the company for their acts. It makes the management more responsible towards their fiduciary duties in relation to the company. The legal backing to a Class Action has given a stronger foothold to the minority shareholders of a company to safeguard their interest through a representative suit. However, this additional power should not be misunderstood as a new technique to hold the company at ransom for their demands.

As compared to other remedies, Class Action is of a more serious nature and involves grave ramifications if the application is found to be made with malafide intentions or does not confirm to the criteria prescribed in the Companies Act. The shareholders or depositors would not be able to easily get away for filing a frivolous or vexatious application. The applicants should carefully weigh their options under different provisions of the Companies Act before proceeding under this section. Considering the stringent quantitative and qualitative screening of all Class Action applications, an alternate remedy under the Companies Act may sometimes prove to be a safer bet for the shareholders and depositors. However, the possibility of a Class Action suit filing is a welcome introduction.

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